

OFFICE OF AUDITS & ADVISORY SERVICES



DGS CONSTRUCTION CONTRACT ADMINISTRATION

FINAL AUDIT REPORT

Chief of Audits: [Juan R. Perez](#)
Senior Audit Manager: [Lynne Prizzia, CISA, CRISC](#)
Senior Auditor: [Franco D. Lopez, CPA, CIA, CISA](#)

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County of San Diego

TRACY M. SANDOVAL
GENERAL MANAGER/
AUDITOR & CONTROLLER
(619) 531-5413
FAX: (619) 531-5219

FINANCE & GENERAL GOVERNMENT GROUP

1600 PACIFIC HIGHWAY, SUITE 166, SAN DIEGO, CA 92101-2422

ASSESSOR/RECORDER/COUNTY CLERK
AUDITOR AND CONTROLLER
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CIVIL SERVICE COMMISSION
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TREASURER-TAX COLLECTOR

February 28, 2013

TO: April Heinze, Director
Department of General Services

FROM: Juan R. Perez
Chief of Audits

FINAL REPORT: DGS CONSTRUCTION CONTRACT ADMINISTRATION

Enclosed is our report on the DGS Construction Contract Administration. We have reviewed your responses to our recommendations and have attached them to the audit report. The actions taken, in general, are responsive to the recommendations in the report.

Thank you for the courteousness and cooperation extended to the Office of Audits & Advisory Services during the course of the audit.

If you have any questions, please contact me at (858) 495-5661.

JUAN R. PEREZ
Chief of Audits

AUD:FDL:aps

Enclosure

c: David Estrella, Deputy Chief Administrative Officer, Community Services Group
Tracy M. Sandoval, Deputy Chief Administrative Officer/Auditor and Controller
Kaye Hobson, Group Finance Director, Community Services Group

INTRODUCTION

Audit Objective The Office of Audits & Advisory Services (OAAS) completed an audit of the Department of General Services' (DGS) Construction Contract Administration. The objective of the audit was to review the adequacy of controls over construction contract administration and project performance.

Background The County annually develops a capital improvement needs assessment to outline ongoing and to plan anticipated capital projects for a five year period. Once approved by the Board of Supervisors, capital projects are budgeted into the Operational Plan which authorizes DGS to commence with project design and contracting. After a project is awarded to a qualified contractor, DGS manages the project to ensure contracted terms are appropriately executed and completed. At completion, DGS performs a formal closeout procedure which ensures that work was appropriately completed and billed.

The management of County-owned and leased facilities is centralized in DGS where capital costs, operating expenses, and ongoing major maintenance needs are evaluated. This also includes the critical function of construction contract administration for the County's capital improvement projects. The DGS Annual Report FY 2011-12 outlines that DGS had accountability for \$811 million of approved and funded capital projects for the fiscal year, the largest of which included:

- County Women's Detention Facility - \$289 million County
- County Operations Center Redevelopment Phase 1B - \$109 million
- County Administration Center Waterfront Park - \$44.2 million
- Rancho San Diego Sheriff Station - \$17.5 million

Audit Scope & Limitations The scope of the audit was limited to evaluating construction contract administration controls as performed by DGS; the audit did not include evaluating actual project costs incurred. The COC Redevelopment project was selected as our sample due to the project's magnitude and cost. As of September 2012, the project had incurred total costs (design, demolition, and construction of Phases 1A and 1B) of \$246 million of the project's budgeted cost of \$262.5 million.

This audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors as required by California Government Code, Section 1236.

Methodology OAAS performed the audit using the following methods:

- Interviewed County and Developer stakeholders.
- Identified and documented controls and assessed risks of the DGS construction contract administration process.

- Reviewed the COC Redevelopment Disposition and Development Agreement (DDA) as well as relevant DGS business process documents.
- Tested controls over DGS' construction contract administration as related to the DDA, which included:
 - Assessing effectiveness of the quality assurance and quality control processes.
 - Reviewing appropriateness of Phase 1A and 1B submissions and fee calculations.
 - Verifying compliance with the competitive bid process as outlined in the DDA.
 - Verifying contractor compliance with insurance requirements as outlined in the DDA.
 - Verifying compliance by the contractors in obtaining and maintaining all necessary performance and payment bonds in accordance with the DDA.

AUDIT RESULTS

Summary

Within the scope of the audit, OAAS found that DGS controls over construction contract administration and project performance were generally adequate. However, specific issues were identified in the areas of contractor fee computation and bond coverage.

Finding I:

Overbilled Contractor Fee for Phase 1A and Phase 1B

DDA Article I outlines that the contractor fee should be based on the actual cost of work less the Contractor's cost of insurance, bonds, and contingencies.¹ However, at the time of the audit, the Developer had not implemented a process to subtract these costs from the monthly contractor fee billed to the County.

The contractor fees for Phase 1A and Phase 1B were not billed in accordance with DDA. Audit testing identified an overbilling of \$31,088 due to incorrectly calculated contractor fees within the Phase 1A final payment application. Additionally, as outlined in the September 2012 payment application, the contractor fee for Phase 1B had been overbilled by an estimated \$51,800.

Recommendation:

1. DGS should request a refund of the overbilled portion of the contractor fees from the Developer.
2. DGS should strengthen controls by establishing a procedure to ensure that future contractor fee billings are calculated in accordance with the DDA.

¹ DDA Article I Section 1.02(V)

Finding II:**Bond Coverage Not Maintained at Appropriate Amount**

Performance and payment bond coverages were not maintained at the amounts required by the DDA.² The DDA requires that performance and payment bonds “be in an amount equal to 100% (including increases) of the total amount of Developer's contract(s) with the Contractor(s).” However, at the time of the audit, the Developer indicated that bond coverages were only updated when contract values had a significant change. As a result, there is an increased risk that bond coverage will not be sufficient if not updated as required by the DDA.

Recommendation:

To ensure compliance with DDA bond requirements, DGS should strengthen their monitoring procedures to ensure that performance and payment bonds are maintained at 100% of the Developer's agreements with its Contractors.

² As outlined in DDA Article XI Section 11.03, a performance bond is a corporate surety bond whose purpose is to guaranty the faithful performance of the construction work; a payment bond is a surety bond that secures payment of the claims of laborers, mechanics, and material suppliers employed under the DDA.

Office of Audits & Advisory Services

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DEPARTMENT'S RESPONSE



County of San Diego

APRIL F. HEINZE, P.E.

Director
(858) 694-2527
FAX (858) 467-9283

DEPARTMENT OF GENERAL SERVICES

5560 OVERLAND AVE., STE. 410, SAN DIEGO, CA 92123-1204

FACILITIES OPERATIONS
FLEET MANAGEMENT
MAIL SERVICES
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February 15, 2013

RECEIVED

TO: Juan R. Perez
Chief of Audits

FEB 21 2013

FROM: April F. Heinze, P.E., Director
Department of General Services

OFFICE OF AUDITS &
ADVISORY SERVICES

DEPARTMENT RESPONSE TO AUDIT RECOMMENDATIONS: DGS Construction Contract Administration

Finding I: Overbilled Contractor Fee for Phase 1A and 1B

OAAS Recommendation:

1. DGS should request a refund of the overbilled portion of the contractor fees from the Developer.
2. DGS should strengthen controls by establishing a procedure to ensure that future contractor fee billings are calculated in accordance with the DDA.

Action Plan:

- Directed Lowe Enterprises to have Suffolk Roel Construction generate a credit of \$82,888; \$31,088 as a credit in the October 2012 developer pay request and \$51,800 as a correction in the upcoming COC Phase 1B GMP #7 Cost Proposal.
- Monitor future fee calculations in Lowe Enterprises submitted monthly budget forecasts and check future pay request for appropriate fee calculations, in accordance with the DDA.

Planned Completion Date:

- Received and approved the October 2012 developer invoice showing reconciliation of overbilling, with a credit of \$31,088 to the County.
- COC Phase 1B GMP #7 containing the \$51,800 credit correction to the contract amount to be issued during February 2013.

Contact Information for Implementation: Jeff Redlitz, Project Manager (858) 694-8834.

Finding II: Bond Coverage Not Maintained at Appropriate Amount

OAAS Recommendation:

MISSION: To provide cost-effective, efficient, high quality and timely support services to County departments, groups and agencies

1. To ensure compliance with DDA bond requirements, DGS should strengthen their monitoring procedures to ensure that performance and payment bonds are maintained at 100% of the Developer's agreements with its Contractors.

Action Plan:

- Require that performance and payment bonds are updated and maintained at 100% of Developer's agreement with contractors.
- Proof of bonding capacity will be issued quarterly or at the issuance of every DDA contract amendment or Guaranteed Maximum Price (GMP) issuance.

Planned Completion Date:

- Bonds were updated at latest issuance of COC Development contract Phase 2A GMP #3, dated December 12, 2012.

Contact Information for Implementation: Jeff Redlitz, Project Manager (858) 694-8834.

If you have any questions, please contact me at 858-694-2527.


APRIL F. HEINZE, P.E., Director
Department of General Services